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FISCAL IMPACT STATEMENT

LS 7255
BILL NUMBER: HB 1414

NOTE PREPARED: Jan 31, 2013
BILL AMENDED: Jan 31, 2013

SUBJECT: Indiana New Markets Jobs Act.

FIRST AUTHOR: Rep. Crouch
FIRST SPONSOR:

BILL STATUS: CR Adopted - 1st House

FUNDS AFFECTED: X GENERAL
DEDICATED
FEDERAL

IMPACT: State

Summary of Legislation: This bill establishes a New Markets Job Growth Credit (NMJG) against state tax liability for investments made by a taxpayer in a qualified community development entity (CDE) that then uses the proceeds of the investment to make investments in qualified active low income community businesses located in Indiana.

The bill requires a CDE to pay a nonrefundable application fee of $5,000 for each qualified equity investment (QEI) that they seek to have approved by the Indiana Economic Development Corporation (IEDC). The tax credit equals an applicable percentage multiplied by the purchase price of the QEI. The bill requires the IEDC to limit the monetary amount of QEIs to an amount necessary to limit the claiming of the tax credit to not more than $20 M per state fiscal year. The limit is based on the anticipated use of the tax credits without regard to the potential for taxpayers to carry forward unused balances to future tax years.

The bill provides that the IEDC is required to issue letter rulings requested by taxpayers, similar to private letter rulings issued by the Internal Revenue Service at the federal level, regarding the NMJG that will bind the Department of State Revenue, the IEDC, it's agents, and their successors.

Effective Date: January 1, 2013 (retroactive).

Explanation of State Expenditures: *Department of State Revenue (DOR):* The DOR will incur some administrative expenses relating to the revision of the tax form instructions and software programs to implement this bill. The DOR's current level of resources should be sufficient to implement the program.

Indiana Economic Development Corporation (IEDC): The IEDC will incur additional expenses to establish this program. The IEDC will be required to develop an application, process applications, certify community investments, and monitor investment projects.

The bill also requires the IEDC to issue letter rulings to taxpayers regarding the New Markets Job Growth (NMJG) Tax Credit. A letter ruling is a written interpretation of tax law issued to a private individual. The bill states the IEDC has 60 days to respond to a request, but the IEDC may decline for good cause. The letter ruling binds the DOR, the IEDC, and it's agents until the taxpayer claims all the taxpayer's NMJG credits. In addition, the letter ruling only applies to the requesting taxpayer.

While the IEDC's current level of resources should be sufficient to implement the program, any additional administrative cost could be offset by the nonrefundable $5,000 application fee that applicants for the NMJG credit must pay to the IEDC.

Explanation of State Revenues: *Summary*- The New Markets Job Growth Income Tax Credit (NMJG) is designed to attract private investments in economically distressed neighborhoods. The total credit equals 39% of the Qualified Equity Investment (QEI) made by a qualified Community Development Entity (CDE) and is claimed over a seven-year period. Each year, the taxpayer applies the appropriate percentage to the QEI to determine the annual credit amount:

1. 0% for the first and second year
2. 7% for the third year
3. 8% for the fourth, fifth, sixth, and seventh year

The bill goes into effect in CY 2013. NMJG credits can be awarded for QEIs made in that year. The fiscal impact of credits awarded in CY 2013 will occur in FY 2016 due to the applicable percentage tiers. The estimated revenue loss in FY 2016 is approximately $4.3 M with the estimated revenue loss totaling $9.2 M in FY 2017. The usage of the credit will continue to grow until it reaches full utilization of $20 M per fiscal year.

Background - To receive the credit, a taxpayer must file an application in the IEDC and include a $5,000 nonrefundable fee. The IEDC will make a determination within 30 days upon receipt of the application and fee. The credit can be used to offset tax liabilities from the Individual Adjusted Gross Income Tax, Corporate Adjusted Gross Income Tax, Financial Institutions Tax, and Insurance Premiums Tax. Revenue collected from those taxes are deposited in the General Fund. The revenue to the state General Fund would be reduced by the amount of the credits.

The credit is nonrefundable, but the taxpayer may carry forward unused balances for up to five years. In addition, IEDC must limit the amount of QEIs so the total NMJG credits do not exceed $20 M in any fiscal year. This limit is based on the anticipated use of the credits. However, the IEDC does not have to take into account taxpayers who may be carrying forward tax credits.

The Center for Business and Economic Research at Ball State University conducted a study on the effectiveness of the federal New Markets Tax Credit Program (NMTC) and how a state-level version of the NMTC affected overall levels of investment. The study found that states with their own version of a New Markets Tax Credit had higher levels of NMTC investments. They ran a simulation on the impact of Indiana implementing a 39%

state version of the NMTC. The simulation estimated that an Indiana NMTC would attract $433 M dollars in investments over a seven-year period. That is an average of $61 M in QEIs per year.

However, the model results were based on the federal NMTC. The federal program does not require applicants to pay a fee to apply for the credit.

Assuming Indiana attracts a total of $61 M per year in QEIs beginning in CY 2013, the first year the NMJG credits for those investments may be used to offset a tax liability is FY 2016. This is due to the applicable credit percentage tiers.

The NMJG tax credit amount is spread over a seven-year period. The taxpayer may not use the NMJG credit for the first two years following the qualifying investment. Then, the credit equals 7% of the qualifying investment in year three and 8% of the qualifying investment in year four, five, six, and seven. So, the last year an NMJG tax credit could be claimed for a qualifying investment made in CY 2013 would be FY 2020. Applying the applicable credit percentage tiers to an estimated annual amount of qualifying investment of $61 M, the estimated cost of the NMJG tax credit is $4.2 M in FY 2016 and $9.2 M in FY 2017. Under these assumptions, the annual fiscal year limit of $20 M in NMJG credits would be reached in FY 2020 after five years of qualifying investments.

Additional Background-Federal New Markets Tax Credit Program: This bill is based on the NMTC Program. This was enacted by Congress as part of the Community Renewal Tax Relief Act of 2000 and is incorporated as section 45D of the Internal Revenue Code. This Code section permits individual and corporate taxpayers to receive a credit against federal income taxes for making qualified equity investments (QEIs) in qualified community development entities (CDEs).

These investments are expected to result in the creation of jobs and material improvement in the lives of residents of low-income communities. Examples of expected projects include financing small business, improving community facilities such as daycare centers, and increasing home ownership opportunities. The Indiana NMJC uses the same language to determine a qualifying project except the Indiana program excludes charter schools and businesses who derive over 15% of their annual revenue through the rental or sale of real estate.

The actual cash investment made by the investor to the CDE, which is referred to as the equity investment, is the first step in defining a QEI. The cash investment eventually qualifies for the NMTC provided that the CDE makes qualified low-income community investments.

A QEI is, in general, any equity investment in a CDE if:

(1) Such investment is acquired by the investor at its original issue (directly or through an underwriter) solely in exchange for cash;
(2) Substantially all (at least 85%) of the cash is used by the CDE to make a qualified low-income community investments; and
(3) The investment is designated CDE as a QEI on its books and records using any reasonable method.

A taxpayer holding a qualified equity investment on a credit allowance date occurring during the taxable year may claim the NMTC for such taxable year in an amount equal to the applicable percentage of the original purchase price of the QEI. The credit period for the investment is the seven-year period beginning on the date a QEI is initially made, even though the credit is allowable on the first day of each credit year.

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue; Indiana Economic Development Corporation.

Local Agencies Affected:

Information Sources: Hicks, Michael J. And Dagney Faulk. "*The Effect of State-Level Add-On Legislation to Federal New Market Tax Credit Program.*" February 2012; Internal Revenue Service, "*New Markets Tax Credit.*" May 2010; Community Development Financial Institutions Fund, U.S. Department of the Treasury, http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5

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